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No. 05-1335

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SUPREME COURT, U.S.

In The
Supreme Court of the United States

Trustee DARRYL S. LADDIN of the
ETS Creditors' Litigation Trust,

Petitioner,

v.

RELIANCE TRUST COMPANY, PENSCO, INC.,
JOHN PROKOP, and COMMUNITY NATIONAL BANK,

Respondents.

**On Petition For Writ Of Certiorari
To The United States Court Of Appeals
For The Eleventh Circuit**

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether the Eleventh Circuit Court of Appeals ruling that the defense of *in pari delicto* is applicable against a bankruptcy trustee who has succeeded to the interests of a debtor pursuant to 11 U.S.C. § 541(a) warrants review by this Court.

2. Whether the Eleventh Circuit Court of Appeals ruling that the defense of *in pari delicto* is applicable to causes of action arising under the federal Racketeer Influenced and Corrupt Organizations (RICO) Act, 18 U.S.C. § 1961, *et seq.*, warrants review by this Court.

PARTIES

The caption of the Petitioner's Petition contains the names of all the remaining interested parties to this action.

CORPORATE DISCLOSURE STATEMENT

Community National Bank is a wholly owned subsidiary of Community Bancshares, Inc.

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PRIOR CITATIONS AND REPORTS

The Order of the United States District Court for the Northern District of Georgia is not reported. The Eleventh Circuit Court of Appeals decision is reported at 437 F. 3d 1145 (11th Cir. 2006).

STATEMENT OF JURISDICTION

The Order of the Eleventh Circuit Court of Appeals was entered on January 30, 2006. Petitioner filed his Petition for Writ of Certiorari on April 14, 2006. This Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 1254, as a timely appeal of a final decision of a United States Court of Appeals.

STATUTORY PROVISIONS AT ISSUE

1. Federal Racketeer Influence and Corrupt Organizations Act. 18 U.S.C. § 1961 *et seq.*

2. United States Bankruptcy Code. 11 U.S.C. § 541(a).

STATEMENT OF THE CASE

According to the Trustee's Complaint in this matter, in approximately October of 1994, Charles Edwards ("Edwards") formed ETS Payphones, Inc. ("ETS"). (R8-127-17) Trustee's Complaint further alleges, "[w]ith Edwards at its helm, ETS devised the scheme and promoted and marketed the sale and leaseback of payphones as investment opportunities to individuals." (R8-127-18) ETS was in the

business of selling pay coin operated telephones and leasing them back from the customers for a stated amount. (R8-127-17) Edwards, the CEO, founder, and sole shareholder of ETS developed the sale and leaseback business plan. (R8-127-18) According to the Third Amended Complaint, "this business plan was fundamentally flawed from the outset and constituted a fraud on the thousands of investors who entrusted their nest eggs to Edwards." (R8-127-18) The operation of the sale-leaseback program was a Ponzi scheme that defrauded thousands of investors of over $300 million. As the sole shareholder of ETS, Edwards transferred the proceeds from ETS to himself or other companies he owned.

On September 11, 2000, ETS filed for bankruptcy. The bankruptcy court allowed the creation of an Official Committee of Unsecured Creditors, and the Debtors and Creditors' Committee created the ETS Creditors' Litigation Trust. The committee appointed Laddin as trustee of the debtor estate.

Laddin sued several defendants, including Reliance Trust Co., PENSCO, Inc., and Community National Bank, ("IRA Custodians") for among other claims, violations of section 1962(c) and (d) of RICO, 18 U.S.C. §§ 1962(c) and (d). Laddin alleged that these IRA Custodians aided ETS in defrauding investors by funneling investor IRA funds into ETS payphone investments.

The IRA Custodians moved to dismiss Laddin's complaint. They argued Laddin, as trustee, could not maintain his claims based, inter alia, on the doctrine of *in pari delicto*. The district court granted the motions to dismiss and the Eleventh Circuit Court of Appeals affirmed the dismissal.

SUMMARY OF THE ARGUMENT

The Petitioner Trustee, who stands in the shoes of ETS, cannot assert claims that ETS could not have asserted. The Trustee's authority to bring this lawsuit are limited by the clear language of 11 U.S.C. § 541, and are derived, if at all, from the rights he obtained through the Litigation Trust Agreement. As such, the Eleventh Circuit Court of Appeals was correct in ruling the defense of *in pari delicto* is applicable against a bankruptcy trustee who has succeeded to the interests of a debtor pursuant to 11 U.S.C. § 541(a). This ruling is consistent with all the circuit courts that have considered such issue.

Additionally, based on the plain language of 11 U.S.C. § 541(a), the Eleventh Circuit Court of Appeals did not need to consider the legislative history of Section 541 in determining the defense of *in pari delicto* barred the Trustee's claims. Further, the Court of Appeals was correct in finding that even considering the legislative history of Section 541, the defense of *in pari delicto* would still bar the Trustee's claims. The Trustee misconstrued the legislative history of Section 541 and the portion cited by the Trustee is inapplicable to the issues before this Court.

Moreover, the Court of Appeals was correct in finding the defense of *in pari delicto* is applicable to causes of action arising under the federal Racketeer Influenced and Corrupt Organizations (RICO) Act, 18 U.S.C. § 1961, *et seq.*, because RICO violations necessarily require affirmative wrongdoing, such as engaged in by ETS in this instance.

ARGUMENT AND CITATIONS OF AUTHORITY

I. The Court of Appeals was correct in ruling the Trustee's claims against the IRA Custodians are barred by the *in pari delicto defense* and such ruling is consistent with the ruling of every other Circuit Court that has considered the issue and does not merit review by this Court

In their briefs before the District Court and the Eleventh Circuit Court of Appeals, Community National Bank and the other IRA Custodians cited numerous cases wherein the complaints of trustees or creditors' committees against third-parties for their alleged role in aiding or abetting the sole shareholder(s) of a corporation involved in a Ponzi scheme were dismissed based on the doctrine of *in pari delicto*.[1]

Conversely, the Trustee has not identified a single case on point where the court ruled in favor of the Trustee's position and found the *in pari delicto* defense was inapplicable to bankruptcy trustees in such instances. Rather, the Trustee relies instead on commentators who, while acknowledging that the law is as the Court of Appeals determined, none the less advocates a change in the law to preclude the application of the *in pari delicto*

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[1] *See, e.g., In re The Mediators Inc.*, 105 F.3d 822 (2nd Cir. 1997); *Hirsch v. Arthur Andersen & Co.*, 72 F.3d 1085 (2nd Cir. 1995); *E.F. Hutton & Co. v. Hadley*, 901 F.2d 979 (11th Cir. 1990); *Shearson Lehman Hutton Inc. v. Wagoner*, 944 F.2d 114 (2nd Cir. 1991); *F.D.I.C. v. Ernst & Young*, 967 F.2d 166 (5th Cir. 1992); *In re The Mediators Inc.*, 190 B.R. 515 (S.D.N.Y. 1995); *In re Complete Management Inc.*, 2003 WL 21750178 (S.D.N.Y. 2003); *Lippe v. Bairnco Corp.*, 218 B.R. 294 (S.D.N.Y. 1998); *In re Meridian Asset Mgmt. Inc.*, 296 B.R. 243 (N.D. Fla. 2003); *Brown v. Deloitte & Touche LLP*, 1999 WL 269901 (S.D.N.Y. 1999); *Official Committee of Unsecured Creditors of Color Tile, Inc. v. Coopers & Lybrand LLP*, 322 F.3d 147 (2nd Cir. 2003).

defense to bankruptcy trustees. In fact, the Trustee admits in his Petition "the Eleventh Circuit here, *and indeed all of the Circuit Courts that have addressed the question to date . . .* " have determined the defense of *in pari delicto* is applicable to a bankruptcy trustee in this circumstance. (Petitioner's Petition for Writ of Cert., pg. 8).

Moreover, in an attempt to bring this case under the guise of review by this Court, the Trustee asserts "The Eleventh Circuit's 'ruling' that Section 541 is so 'unambiguous' as to *prohibit* consideration of its legislative history creates a split in the Circuits, and a departure from prior rulings by this Court, on that issue." (emphasis added) (Petitioner's Petition for Writ of Cert., pg. 12).

Contrary to the Trustee's assertions, the Eleventh Circuit did not issue a "ruling" or holding "prohibiting" consideration of the legislative history of Section 541(a). Rather, the Eleventh Circuit merely stated in its analysis of the applicability of the *in pari delicto* defense under Section 541(a) that it "need not resort to legislative history" due to the "unambiguous" language of Section 541(a) with regard to the particular issue before it. *Laddin v. Edwards,* 437 F.3d 1145, 1150 (11th Cir. 2006). In fact, the Eleventh Circuit did consider the legislative history of Section 541(a) and undertook a rather detailed analysis of such history and reached the same conclusion it reached based on its analysis of the language of the statute itself, a conclusion the Trustee readily admits has been reached by every other circuit court that has considered the issue.

Further, the Trustee seeks review by this Court of the Eleventh Circuit's decision based on "equitable principles" in the bankruptcy code not considered by the Court. The Trustee argues the Eleventh Circuit, in issuing its ruling,

"refused to consider the post-petition removal of the wrongdoer (Edwards) and appointment of an innocent party (the Trustee) seeking recovery for the benefit of innocent investors and other creditors." The Trustee again mischaracterizes the Eleventh Circuit's Opinion in his attempt to gain review by this Court.

Contrary to the Trustee's assertions, the Eleventh Circuit specifically addressed the "equitable principles" espoused by the Trustee in his Petition. The Eleventh Circuit specifically stated in its Opinion:

> Laddin argues that his recovery would ultimately inure to the benefit of innocent creditors instead of the wrongful debtor, but he fails to account for the likelihood that individual creditors damaged by the debtor's Ponzi scheme could separately pursue claims against the IRA Custodians free from the bar of in pari delicto.

Id. at 1151. The mere fact the Trustee may not like or agree with the Eleventh Circuit's ruling regarding this matter is an insufficient basis to seek review of that ruling by this Court. The Eleventh Circuit was correct in both its analysis, and its conclusions, regarding the issues before it in this case and there is no split in the Circuits regarding any issues that were before it that merit review by this Court.

II. The Court of Appeals was correct in ruling the defense of *in pari delicto* is applicable to causes of action by a conspirator arising under the federal Racketeer Influenced and Corrupt Organizations (RICO) Act, 18 U.S.C. § 1961, *et seq.* and such ruling does not merit review by this Court.

The Trustee asserts the ruling by the Eleventh Circuit that the defense of *in pari delicto* bars the Trustee's claims against Commercial National Bank and the IRA Custodians is contrary to the rulings of "numerous" other federal courts and as such, should be reviewed by this Court. Contrary to Trustee's assertion however, federal case law regarding this issue is scarce, and no other circuit court has directly determined this issue.

This Court has however, as stated by the Eleventh Circuit in its Opinion, considered the issue of the application of the *in pari delicto* defense in the context of federal antitrust and securities regulations. *Bateman Eichler v. Berner*, 472 U.S. 299, 105 S. Ct. 2622, 86 L. Ed. 2d 215; *Perma Life Mufflers, Inc. v. Internat'l Parts Corp.*, 392 U.S. 134, 88 S. Ct. 1981, 20 L. Ed. 2d 982 (1968). As admitted by the Trustee in his Petition, federal law governs the applicability of affirmative defenses, such as *in pari delicto*, to causes of action created by federal law. *See O'Melveny & Myers v. FDIC*, 512 U.S. 79, 84-85, 114 S. Ct. 2048, 2053, 129 L. Ed. 2d 67 (1994).

As pointed out by the Eleventh Circuit, pursuant to the *Perma Life Mufflers* and *Bateman Eichler* Opinions, the application of the *in pari delicto* defense to federal causes of action, including RICO, depends on two factors: (1) the plaintiffs' active participation in the violation vel non and (2) the policy goals of the federal statute. *Laddin v. Edwards*, 437 F.3d at 1154. In his Petition, Trustee does not take issue with the Eleventh Circuit's pronouncement of these factors. Rather, the Trustee asserted the Eleventh

Circuit "drew ill-founded distinctions" between this case and the *Perma Life Mufflers* and *Bateman Eichler* cases, and misapplied this Court's rulings in those cases under the context of the RICO act.

While Community National Bank strongly disagrees that the Eleventh Circuit misapplied the factors set forth by this Court in *Perma Life Mufflers* and *Bateman Eichler*, the misapplication of these factors by the Eleventh Circuit, even if such did occur, is not a sufficient basis for review of the Eleventh Circuit's Opinion by this Court. United States Supreme Court Rule 10 specifically states, "A petition for writ of certiorari is rarely granted when the asserted error consists of erroneous factual findings *or the misapplication of a properly stated rule of law.*" Thus, while review on a write of certiorari is discretionary, the assertions by Trustee in his Petition do not allege a basis for which this Court has historically granted review and the Trustee's Petition should be denied.

CONCLUSION

For all of the reasons set forth herein, Respondent Community National Bank prays that Petitioner Trustee's Petition for Writ of Certiorari be denied.

Respectfully submitted,

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